DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 02-0573
Adjusted Gross Income Tax
For the Tax Period 1998

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ISSUE

1. Adjusted Gross Tax-Imposition

Authority: IC 6-8.1-5-1(b), IC 6-3-2-1(a), IC 6-3-2-2.5(a).

The taxpayer protests the assessment of adjusted gross income tax on certain receipts.

STATEMENT OF FACTS

The taxpayer is a married couple. They filed their Indiana tax return and paid their total Indiana adjusted gross income tax liability for 1996-1998. Subsequently the Internal Revenue Service audited the taxpayer's federal return for the years 1996-1998. The audit resulted in two adjustments increasing the taxpayer's federal adjusted gross income tax liability. The taxpayer paid one liability and negotiated a settlement with the Internal Revenue Service (IRS) to satisfy the other federal liability. The IRS notified the Indiana Department of Revenue (department) of the federal audit adjustments for the three year period. The department then recalculated the taxpayer's Indiana income tax liability based upon the federal changes for the tax year 1998. The taxpayer agreed with one of the adjustments and paid the resulting tax liability. The taxpayer protested the assessment of tax, interest, and penalty based on the other adjustment. A hearing was held and this Letter of Findings results.

1. Adjusted Gross Income Tax-Imposition

Discussion

As a result of the IRS audit, the taxpayer's federal adjusted gross income was changed for the years 1996-1998. Since the Indiana adjusted gross income is determined by modifying the federal adjusted gross income tax, the change in the federal adjusted gross income tax required a corresponding change in the Indiana adjusted gross income tax. The taxpayer did not make this change and amend its returns for the years of the federal tax audit. The department became aware of the federal adjustments and made the corresponding adjustment in the taxpayer's Indiana gross income for 1998. The adjustment in the taxpayer's Indiana adjusted gross income resulted in a deficiency of

Indiana income taxes paid in 1998. The department's recomputation of the 1998 income tax based upon the adjusted Indiana adjusted gross income tax was proper.

After the federal audit, the taxpayer filed an action against the IRS to recover the additional federal income taxes it paid pursuant to the audit. This lawsuit was settled with the United States Government refunding the taxpayer fifty percent (50 %) of the taxes they had paid as a result of the audit. The taxpayer argues that since they settled with the IRS for fifty (50) cents on the dollar, the department should correspondingly reduce their Indiana adjusted gross income tax liability by fifty percent (50%).

All department assessments are prima facie evidence that the taxes are owed by the taxpayer who has the burden of proving that the assessment is incorrect. IC 6-8-1-5-1(b). Indiana imposes the adjusted gross income tax on Indiana residents. IC 6-3-2-1(a). The Indiana adjusted gross income is calculated by starting with the federal adjusted gross income and making certain statutory modifications. IC 6-2-2.5(a).

The department disagrees with the taxpayer's conclusions. The settlement documents presented in association with the hearing give no indication that the IRS ever actually reduced the taxpayer's federal adjusted gross income. Rather, the settlement documents states specifically that the parties are "willing to settle this matter for fifty (50%) percent of the amount paid, plus statutory interest from January 2, 2002." At no point does the settlement documentation indicate that the taxpayer's actual federal adjusted gross income was reduced.

The department properly calculated the taxpayer's Indiana adjusted gross income tax based upon the taxpayer's federal adjusted gross income as reflected in the Revenue Agent's Report associated with the federal adjusted gross income tax audit for the tax year 1998.

<u>FINDING</u>

The taxpayer's protest is denied.

KMA/PE/JMS/05/12/2005